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DEPARTMENT FOR AF/W AND AF/EPS
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TAGS: ECON EMIN ETRD EFIN PREL BEXP SL

SUBJECT: LARGEY U.S.-OWNED SIERRA RUTILE OFF TO GOOD

START: TOP POLITICAL LEADERSHIP FAVORABLE

Classified By: CHARGE D'AFFAIRES JAMES A. STEWART FOR REASONS 1.4 B/D.

Summary

¶1. (C) Sierra Rutile (SR) just exported the first shipment of mined product since 1995. Board members, including Chairman Walter Kansteiner, witnessed the re-entry of the US.-owned company into world markets. Up until the mid-1990s when the mining equipment was destroyed by rebels, SR was the world's largest rutile operation. SR will export 10,000 tons per month worth \$4.5 million and for three months has been exporting bauxite mined nearby worth \$2.5-3.0 million per month. High oil prices are hurting the bottom line as the mines depend on thermally generated electricity. SR is looking at alternative fuels, including from algae grown in ponds left by mining operations. SR offered its stock on the London exchange in 2005 and shows a market value of \$325 million. Board members explained that they are seeking \$70 million in financing for capital equipment, including dredges, generators, barges, and port equipment. To that end they are talking to OPIC and the EX/IM Bank as well as contemplating a further stock offer. Executives report that relations with local government and labor are good. They have 18 months to implement their obligatory land recovery plan. In a May 8 meeting, President Kabbah vowed to keep the MOU and its tax concession intact and VP Berewa followed suit separately. Under the MOU, SR will transfer 30 percent of its stock to the Government over a 10-year period. A National Revenue Authority (NRA) official told post that there is no intention to alter the MOU or tax concessions, but wants SR to pay up on the 1 percent tax levied in exchange for all other taxes being waved. Top official understand, even if mid-level tax and other functionaries do not always, how SR's success benefits the economy and Sierra Leone's reputation as a place to do business. End Summary.

Kansteiner and Board Members Witness First Export Shipment

¶2. (U) On May 8, Sierra Rutile (SR) shipped its first load of rutile out of Sierra Leone since 1995. The shipment, bound for the Netherlands, coincided with a visit to Sierra Leone of some members of the U.S.-owned company's Board of Directors, including Chairman (and ex-A/S for African Affairs) Walter Kansteiner. Local company executives showed the visitors current operations and recent progress on the ground at the rutile mine and the nearby allied bauxite operation. A decade ago, SR was the largest rutile producer in the world until the mining equipment and plant were destroyed in the rebel war.

\$7 Million in Monthly Exports Large for Sierra Leone

¶3. (U) The company is on track to export 10,000 tons of rutile per month at \$450/T for monthly revenues of \$4.5

million and is ready in the next year or two to double output. Company executives said that the market will bear such an increase as Sierra Leonean rutile is known for its purity and high quality. The company has been exporting bauxite for the past three months at the rate of 100,000 tons per month. Those exports fetch \$25-30 per ton, depending on the customer, implying a monthly gross income stream of \$2.5)3.0 million. Company managers related that current bauxite exports are going to Alcoa in Texas.

¶4. (U) Rutile is titanium oxide which is an important ingredient in paints and welding rods. Rutile sands are found in deposits along old river beds where they have collected in geological time. They are dredged up then go through preliminary centrifuge processing to separate out rocks and clay and leave heavy dark-colored rutile sands. The high-concentrate rutile ore, which constitutes the majority of the sands, is then separated via an electrostatic process. The lower quality sands also find an export market.

Zirconium is present in limited quantities and there is a ready world market for that high value metal as well as for other minerals in low concentrations. Bauxite mining and processing is less complex. Both products are shipped by rail to the shallow port of Nitti in southwestern Sierra Leone where they are barged to a ship waiting in deeper water offshore.

High Fuel Costs Hurting Balance Sheet

¶5. (SBU) The run-up in world oil prices is hurting SR's bottom line. The mines operate entirely on electricity generated by an on-site thermal plant. With diesel fuel prices up 208% in the past year, fuel costs are making the company run deeper in the red than financial projections

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predicted, according to Sierra Rutile management.

¶6. (U) In order to cope with the problem, SR executives are considering a number of alternative energy sources. In the near term, they plan to switch from diesel to less expensive, but dirtier, liquid heavy fuel, which will require the purchase of new generators. Over the longer run, they are considering more innovative solutions, including generating bio-diesel and cellulosic ethanol from local oil palm plantations as well as bio-fuel created from algae grown in pools left by the mining operations.

¶7. (U) Biological scientists have explained to post that algae is more proficient energy producer per unit volume than other bio-fuels. An added advantage is that algae fuel can be used with straight forward add-ons to existing plant and does not require radical retro-fitting. Even if algae development were to take several years, with a predicted mine life span of 30 years, company managers recognize that such an alternate energy input to the mines and associated plants could reduce significantly their energy bill. Non-executive SR board member Rod Baker told PolOff that in late May he will bring a University of Arizona scientist to evaluate the potential for algae-based bio-fuel production.

Seeking Expansion Capital

¶8. (SBU) Sierra Rutile offered its stock in an Initial Public Offering (IPO) on the London exchange in 2005. The stock has enjoyed solid growth since and shows a company market capitalization of \$325 million. The board of directors and management are considering returning to the London exchange for additional capital but they are also talking to OPIC and the EX/IM Bank about financing capital equipment. They say they need \$70 million for added dredges, new generators, new barges, and a revamped port facility at Nitti. Kansteiner and the board are optimistic that EX/IM Bank will look favorably on new dredges and large generators if they are of US manufacture.

Good Relations with Local Government and Labor

¶19. (SBU) The company makes regular payments to local chiefs and local councils, amounting to \$400,000 per annum for the rutile lands and \$100,000 from the bauxite lands. As management explained, it is the political process that determines who receives the rents: the company simply writes the check to whom the Government designates.

¶10. (SBU) Sierra Rutile recently signed a labor contract with the mine workers union. Company executives reported good labor relations and also that they are happy with bargain they struck with the 2,000 workers in the rutile and bauxite mines operations, processing plants, and in shipping.

¶11. (C) Company officials noted that local politics and chieftancy loyalties are colored by the divide between, on the one hand, VP Berewa and the ruling SLPP to which he belongs, and, on the other hand, Charles Margai and his breakaway PMDC party. They added that they have to be careful not to be drawn into such political squabbles.

Land Recovery Plan in Place

¶12. (U) Company executives said that recovering mined land is important. At present, some of the ponds created by rutile mining are being used to grow tilapia fish for local consumption. The pond water has been tested and reportedly is clean and potable. Kansteiner told PolOff that local communities now rely on the fish for protein, and Bird Life International has indicated interest in researching some of the exotic bird species attracted to the pools. SR has 18 months to implement their obligation to rehabilitate mined-out lands. Before doing so, SR plans to work through the mine tailings left by earlier operations under Bethlehem Steel. Company managers explained that the land rehab plan consists of creating more tilapia ponds or returning the land to agricultural use.

Paying Fees, Getting Some Tax Breaks, Leave MOU As Is

¶13. (SBU) The MOU between SR and the Government specifies certain tax concessions. Nevertheless, Sierra Rutile pays fees to the national port authority even though it built and owns the port of Nitti where it ships rutile and bauxite and receives necessary equipment and supplies.

¶14. (U) The MOU also specifies that the company will transfer

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to Government ownership one-third of its stock in the first 10 years of operation and company leadership said they are committed to doing so.

¶15. (C) Earlier on May 8, President Kabbah expressed pleasure with the foreign investment in Sierra Leone and applauded the success of the company to Kansteiner and board members and company managers. Underscoring that SR is operating in the red and will continue to show losses for a few years until production is ramped up and costs are driven down, company representatives reported making a strong case to Kabbah for the Government to leave the MOU as is and to continue the existing tax concessions. Kabbah, they said, accepted that the MOU should not be changed. Later the same day, Vice President Berewa gave similar strong support for SR and the existing MOU.

¶16. (SBU) Sierra Rutile officials report that some in the Government and bureaucracy want to change concessionary elements of the MOU and tax the company much more heavily. In the local context, some authorities see SR as a large and rich company and, on that basis alone, should be taxed. A National Revenue Authority (NRA) official told us, however, that there was no desire on the Government's part to modify SR's existing tax concessions, rather the NRA wants SR to pay up under that agreement. He explained that per Sierra

Leonean regulations, SR owes a 1 percent concessionary tax, in lieu of other taxes that SR is not required to pay. He noted, that that rate is below even the normal rate for tax exempt entities which usually must pay a 1.5 percent service charge.

Comment

¶17. (C) The Government is under pressure from the IMF and World Bank to increase its own revenue base via taxes and fees. Under (relatively) new Finance Minister John Benjamin the National Revenue Authority (NRA) has become much more aggressive in recent months. At a reception for Sierra Rutile, Benjamin called on the NRA to get after Sierra Rutile) he was only half joking. The FinMin has upped an array of taxes, including fuel taxes and a &service charge8 applied also to diplomatic missions for port clearance that violates international conventions. After their conversations with President Kabbah and VP Berewa who evinced understanding of the environment international investors need in order to succeed, Sierra Rutile's leadership is confident that the concessions articulated in the MOU are safe while the company amortizes large machinery expenditures and other front-loaded expenditures typical of such a capital intensive undertaking.

By and large, Sierra Leone's political leadership recognizes the positive contribution in job creation and multiplier effects in the economy that Sierra Rutile brings. The top people also recognize, if the mid-level functionaries do not always, that a successful Sierra Rutile makes a substantial contribution to the country's business reputation and by its example helps to attract further investors. End Comment.

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